

Regulation 17053.37-0

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Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.

Regulation 17053.37-1

The Joint Strike Fighter (JSF) Property Credit -- (See Regulation 17053.37-0 for Table of Contents.)

(a) *In General.* The Joint Strike Fighter (JSF) Property Credit is allowed to any qualified taxpayer in an amount equal to ten percent (10%) of any qualified costs paid or incurred on or after January 1, 2001, and before January 1, 2006, for qualified property that is placed in service in this state and used by a qualified taxpayer in qualified activities to manufacture a product for ultimate use in a Joint Strike Fighter. A qualified taxpayer who leases qualified property for use in qualified activities of the qualified taxpayer may also claim the JSF Property Credit. Qualified property may be either new or used and must be placed in service in this state and used by a qualified taxpayer in qualified activities for more than one year to avoid recapture of the JSF Property Credit. The basis of any qualified property for which the JSF Property Credit is claimed is not required to be reduced by the amount of any JSF Property Credit claimed.

(b) *Cross References.* Regulation 17053.37-2 contains definitions applicable to Regulations 17053.37-1 through 17053.37-11, inclusive, Regulation 17053.37-3 contains rules relating to qualified taxpayers, Regulation 17053.37-4 contains rules relating to qualified costs, Regulation 17053.37-5 contains rules relating to qualified property, Regulation 17053.37-6 contains rules applicable to leases of qualified property by qualified taxpayers, Regulation 17053.37-7 contains rules relating to contract bidding, Regulation 17053.37-8 contains recapture rules, Regulation 17053.37-9 contains rules relating to carryforwards, Regulation 17053.37-10 contains general recordkeeping requirements, and Regulation 17053.37-11 contains other miscellaneous provisions. For rules relating to the JSF Property Credit allowed to taxpayers under the Personal Income Tax Law, see Revenue and Taxation Code Section 17053.37 and the regulations thereunder.

(c) *General References.* For purposes of Regulations 17053.37-1 through 17053.37-11, inclusive, the following general references shall apply:

(1) All citations to the Revenue and Taxation Code are to the California Revenue and Taxation Code.

(2) All citations to the Internal Revenue Code are to the Internal Revenue Code of 1986, as amended.

(3) The credits provided for in Revenue and Taxation Code Sections 17053.37 and 23637 shall be collectively referred to as the "Joint Strike Fighter Property Credit" or the "JSF Property Credit."

(4) Any reference to sales or use tax shall mean California sales or use tax imposed under Part 1 (commencing with Section 6001) of Division 2 of the Revenue and Taxation Code. Any discussion of California sales and use tax law in Regulations 17053.37-1 through 17053.37-11, inclusive, is based upon such law as in effect on the date these regulations become effective, and

is generally intended to restate the requirements set forth in Revenue and Taxation Code Section 17053.37 and to be illustrative of, but have no effect on, the California sales and use tax law and the regulations thereunder. All examples which contain references to an amount of California sales or use tax shall be at an assumed hypothetical sales or use tax rate of eight percent (8%).

(5) Unless otherwise provided, any reference to capitalized labor costs in the examples in this regulation shall mean labor costs that are direct costs, as that term is used in Section 263A of the Internal Revenue Code and defined in the regulations thereunder, that can be identified or associated with and are properly allocable to construction or modification of qualified property.

(6) Unless otherwise provided, any reference to qualified property in the examples in this regulation shall assume that the qualified property is being used primarily to manufacture a product for ultimate use in a Joint Strike Fighter. In addition, unless otherwise provided, all examples in this regulation shall assume that the qualified taxpayer's bid to manufacture property for ultimate use in a Joint Strike Fighter reflected a reduction in the amount of the Joint Strike Fighter credit allowable as provided in Revenue and Taxation Code Section 17053.37(i)(2) and Regulation 17053.37-7.

Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.

Regulation 17053.37-2

Definitions – (See Regulation 17053.37-0 for Table of Contents.)

For purposes of Regulations 17053.37-1 through 17053.37-11, inclusive, the following definitions shall apply:

(a) *Capitalized Labor.* The term "capitalized labor" shall mean all costs of labor that are direct costs, as that term is used in Section 263A of the Internal Revenue Code and defined in the regulations thereunder, that can be identified or associated with and are properly allocable to the construction, modification, or installation of specific items of qualified property. For this purpose, labor encompasses full-time and part-time employees, as well as contract employees and independent contractors.

(1) Direct labor costs shall include all elements of compensation, such as basic compensation, overtime pay, vacation pay, holiday pay, sick leave pay (other than payments pursuant to a wage continuation plan under Internal Revenue Code Section 105(d) as it existed prior to its repeal in 1983), shift differential, payroll taxes, and payments to a supplemental unemployment benefit plan, but shall not include any indirect labor costs.

(2) Indirect labor costs are costs that cannot be identified or associated with the construction, modification, or installation of specific items of qualified property. Indirect labor costs include, but are not limited to, training costs, officers' compensation, pension and other

related costs, and employee benefit expenses (including payments pursuant to a wage continuation plan under Internal Revenue Code Section 105(d) as it existed prior to its repeal in 1983).

(3) In determining whether direct costs of labor are properly allocable to the construction, modification, or installation of a specific item of qualified property, the qualified taxpayer shall be required to use the same method of allocation for California income and franchise tax purposes that the taxpayer used for federal income tax purposes under the uniform capitalization allocation rules specified in Treasury Regulation Section 1.263A-1 (as in effect on the date Regulation 17053.37-2 is effective).

(b) *Fabricating*. The term "fabricating" shall mean the process of making, building, creating, producing, or assembling components or property to work or be useable in a new or different manner.

(c) *Joint Strike Fighter*. The term "Joint Strike Fighter" shall mean the next-generation air combat strike aircraft developed and produced under the Joint Strike Fighter program of the United States government.

(d) *Initial Contract or Initial Subcontract*. The term "initial contract" shall mean the contract awarded by the United States government to a prime contractor for any phase, including the Engineering and Manufacturing Development Phase, of the Joint Strike Fighter Program to produce the Joint Strike Fighter Aircraft. The term "initial subcontract" shall mean a contract between a prime contractor and any other contractor, or between two contractors where those contractors have been listed as subcontractors on the bid for the initial contract, or the prime contractor has consented to the contract in writing, to produce a product that is physically attached to or installed in a Joint Strike Fighter Aircraft under the initial contract.

(e) *Joint Strike Fighter Program*. The term "Joint Strike Fighter program" shall mean the multiservice, multinational project conducted by the United States government to develop and produce the next generation of air combat strike aircraft.

(f) *Manufacturing*. The term "manufacturing" shall mean the process of converting or conditioning property by changing the form, composition, quality, or character of the property for ultimate use in a Joint Strike Fighter, and includes any improvements to tangible personal property that result in a greater service life or greater functionality than that of the original property. Tangible personal property shall be treated as having a greater service life if such property can be used for a longer period than such property could have been used prior to the conversion or conditioning of such property. Tangible personal property shall be treated as having greater functionality if it has been improved in such a manner that it can be used to perform new or different functions.

(g) *Packaging*. The term "packaging" shall mean to wrap, seal, box, or put together as a unit, but shall include only that portion of any wrapping, sealing, boxing, or putting together as a unit that is necessary to prepare the goods for delivery to and placement in the qualified taxpayer's finished goods inventory, or to prepare the goods so that they are suitable for delivery

to and placement in finished goods inventory. Additional wrapping, sealing, boxing, or putting together as a unit, such as any wrapping, sealing, boxing, or putting together as a unit that is necessary to consolidate the finished goods prior to shipping or to protect them during transportation, shall not be treated as packaging.

(h) *Placed in Service*. The term "placed in service" shall mean the earliest taxable year in which either of the following occurs:

(1) under the depreciation method used by the qualified taxpayer for California tax purposes, the period for depreciation with respect to the qualified property commences; or

(2) the qualified property is placed in a condition or state of readiness and availability for a specifically assigned function. If qualified property meets the conditions of subsection (h)(2) of this regulation in any taxable year, it shall be considered placed in service in such year, notwithstanding that the period for depreciation with respect to the qualified property begins in a succeeding taxable year. For example, if under the qualified taxpayer's California depreciation practice such qualified property is accounted for in a multiple asset account and depreciation is computed under an averaging convention, or depreciation is computed under the completed contract method, the unit of production method, or the retirement method, then the qualified property is treated as in a condition or state of readiness and availability for a specifically assigned function. Specific examples where qualified property shall be considered in a condition or state of readiness and available for a specifically assigned function include (A) parts that are acquired and set aside during the taxable year for use as replacements for a particular item or items of qualified property in order to avoid operational time loss, (B) operational items of qualified property that are acquired for a specifically assigned function during the taxable year where it is not practicable to use such item of qualified property for its specifically assigned function in the qualified taxpayer's business until the following taxable year, and (C) qualified property acquired for a specifically assigned function that is operational but is still undergoing testing to eliminate any defects. Materials and parts acquired to be used in the construction of an item of qualified property shall not be considered in a condition or state of readiness and availability for a specifically assigned function.

(i) *Product for Ultimate Use in a Joint Strike Fighter*. The term "product for ultimate use in a Joint Strike Fighter" shall mean a product that is physically installed in or attached to a Joint Strike Fighter aircraft. The term "product for ultimate use in a Joint Strike Fighter" shall not include any product that does not form a physical part of the Joint Strike Fighter aircraft.

(j) *Primarily*. The term "primarily" shall mean that property is used 50 percent or more of the time in qualified activities. For purposes of the preceding sentence, the term "time" shall mean the total number of hours that the property is actually in use during the 12-month period immediately following the date the property is placed in service in this state. For example, if an item of property is used by a qualified taxpayer for a total of 100 hours for all uses during the 12-month period immediately following the date the property is placed in service in this state, then "primarily" used in qualified activities means at least 50 hours of the property's use is in qualified activities.

(k) *Process*. The term "process" shall mean the period beginning at the point at which any raw materials are received by the qualified taxpayer and introduced into the manufacturing, processing, or fabricating activity of the qualified taxpayer and ending at the point at which the manufacturing, processing, or fabricating activity of the qualified taxpayer has altered tangible personal property to its completed form, including packaging, if required. Raw materials will be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified taxpayer's manufacturing, processing, or fabricating activity is conducted. Raw materials that are stored on premises other than where the qualified taxpayer's manufacturing, processing, or fabricating activity is conducted, shall not be considered to have been introduced into the manufacturing, processing, or fabricating process.

(l) *Processing*. The term "processing" shall mean the process of physically applying the materials and labor necessary to modify or change the characteristics of property.

(m) *Qualified Activities*. The term "qualified activities" shall mean activities engaged in by a qualified taxpayer that involve manufacturing, processing or fabricating a product for ultimate use in a Joint Strike Fighter.

Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.

Regulation 17053.37-3

Qualified Taxpayer – (See Regulation 17053.37-0 for Table of Contents.)

(a). *In General*. For purposes of Regulations 17053.37-1 through 17053.37-11, inclusive, a qualified taxpayer is any taxpayer under an initial contract or initial subcontract to manufacture property for ultimate use in a Joint Strike Fighter. The term "initial contract" shall mean the contract executed by the United States government and a prime contractor for any phase, including the Engineering and Manufacturing Development Phase, of the Joint Strike Fighter Program to produce the Joint Strike Fighter Aircraft. The term "initial subcontract" shall mean a contract between a prime contractor and any other contractor, or between two contractors where those contractors have been listed as subcontractors on the bid for the initial contract or where the prime contractor has consented to the contract in writing, to produce a product that is physically attached to or installed in a Joint Strike Fighter Aircraft under the initial contract.

EXAMPLE 1: X is awarded the contract for the Engineering and Manufacturing Development Phase of the Joint Strike Fighter Program and executes a contract with the United States government for completion of that phase. Under these facts, X is a qualified taxpayer because X is a prime contractor awarded the initial contract from the United States government for a phase of the Joint Strike Fighter Program.

EXAMPLE 2: Assume the same facts as EXAMPLE 1, except that X and Y are both awarded a portion of the contract for the Engineering and Manufacturing Development Phase of

the Joint Strike Fighter Program and both execute contracts with the United States government for completion of their respective portions of that phase. Under these facts, both X and Y are qualified taxpayers because they are prime contractors awarded initial contracts from the United States government for a phase of the Joint Strike Fighter Program.

EXAMPLE 3: Assume the same facts as EXAMPLE 1, except that Z submits a bid to X, the prime contractor, and is awarded a subcontract to manufacture a product for ultimate use in a Joint Strike Fighter under the scope of the initial contract. Under these facts, Z is a qualified taxpayer because Z is a subcontractor under an initial subcontract for a phase of the Joint Strike Fighter Program.

EXAMPLE 4: Assume the same facts as EXAMPLE 3, except that A submits a bid to Z and is awarded a contract with Z to perform a portion of Z's work under the scope of Z's contract with X. X consents in writing to the contract between Z and A. Under these facts, A is also a qualified taxpayer because A is a subcontractor under an initial subcontract for a phase of the Joint Strike Fighter Program.

EXAMPLE 5: Assume the same facts as EXAMPLE 4, except that A was not listed as a subcontractor on the bid for the initial contract and X does not consent in writing to the contract between Z and A. A thereafter completes all of the work in its contract with Z. Even though A has assisted in manufacturing a product for ultimate use in a Joint Strike Fighter under the scope of the initial contract, A is not a qualified taxpayer because X has not consented in writing to the contract and A is thus not a subcontractor under an initial subcontract for a phase of the Joint Strike Fighter Program.

(b) *Pass-Through Entities.* For purposes of Regulations 17053.37-1 through 17053.37-11, inclusive, in the case of any partnership or S corporation, the determination of whether a taxpayer is a qualified taxpayer shall be made at the entity level. Any credit allowed under Revenue and Taxation Code Section 17053.37 and this regulation shall be passed through to the partners or shareholders in accordance with applicable provisions of Part 10 (commencing with Section 17001) or Part 11 (commencing with Section 23001) of the Revenue and Taxation Code.

Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.

Regulation 17053.37-4

Qualified Costs – (See Regulation 17053.37-0 for Table of Contents.)

(a) *In General.* For purposes of Regulations 17053.37-1 through 17053.37-11, inclusive, the term "qualified costs" includes any costs paid or incurred by a qualified taxpayer for the construction, reconstruction, or acquisition of qualified property on or after January 1, 2001, and before January 1, 2006, provided that California sales or use tax has been paid, directly or indirectly, on such costs (except for costs paid or incurred for capitalized labor), and such costs

are properly chargeable to the qualified taxpayer's capital account. However, the term "qualified costs" does not include the amount of any California sales or use tax paid, directly or indirectly, by the qualified taxpayer.

(b) *California Sales and Use Tax Payment Requirement.* In order for costs to be treated as qualified costs, California sales or use tax must be paid, directly or indirectly as a separately stated contract amount or as determined from the books and records of the qualified taxpayer, with respect to the qualified property. For purposes of Regulations 17053.37-1 through 17053.37-11, inclusive, the requirement that California sales or use tax be paid prior to claiming the JSF Property Credit shall be deemed satisfied as of the date the California sales or use tax is due and payable under Part 1 (commencing with Section 6001) of Division 2 of the Revenue and Taxation Code. In the case of any costs paid or incurred by the qualified taxpayer upon which California sales or use tax has not been paid (except in the case of amounts properly treated as capitalized direct labor for the construction, modification, or installation of qualified property), such amounts shall not be treated as qualified costs. In the case of any leasing transaction, Regulation 17053.37-6 contains special rules applicable to the California sales and use tax payment requirement.

EXAMPLE 1: D, a qualified taxpayer, purchases three hydraulic turbines from B, a California manufacturer of hydraulic turbines, for \$500 to be used in D's manufacturing facility in Escondido. Under the terms of the purchase contract, B agrees to install the turbines at D's manufacturing facility by affixing them to the facility's concrete floor for an additional \$100. Assume \$36 of the \$100 installation charge constitutes direct labor costs paid by B to its employees under Section 263A of the Internal Revenue Code. B charges and collects from D \$40 in California sales tax under the contract ($\$500 \times 8\%$), with the \$100 in installation charges being separately stated in the purchase contract and for purposes of this example are assumed to be exempt from California sales and use tax. Under these facts, D has \$536 in qualified costs (\$500 in costs upon which California sales tax was paid and \$36 in capitalized direct labor costs, but excluding the \$40 in sales tax).

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that instead of D purchasing the turbines from B, D enters into a "fixed-price, turn-key" contract with C, the terms of which require D to pay C a total of \$640 upon delivery and installation of the turbines in D's manufacturing facility. C, instead of delivering a resale certificate to B, pays \$40 ($\$500 \times 8\%$) in California sales tax to B on its purchase of the turbines. Under C's contract with D, the \$40 California sales tax paid by C is a separately stated item. Under these facts, since the sales tax was separately stated in D's contract with C and paid by C on behalf of D, D is treated as having satisfied the California sales tax payment requirement. However, since \$40 of the total contract price represents the sales tax paid indirectly by D, the amount of D's qualified costs is \$536 (\$500 for the turbines plus \$36 in capitalized direct labor costs, but excluding the \$40 in sales tax).

EXAMPLE 3: Assume the same facts as in EXAMPLE 2, except that D's contract with C does not separately state the amount of California sales tax paid by C. However, D's books and records substantiate that C paid California sales tax on behalf of D and that the total contract price of \$640 is broken down between \$500 for the turbines, \$40 in California sales tax, and

\$100 in installation charges. Under these facts, the result is the same as in EXAMPLE 2 since the amount of California sales tax treated as being paid indirectly by D can be determined from D's books and records.

(c) *Capitalization Requirement.* In order for costs to be treated as qualified costs, they must be amounts properly chargeable to the capital account of the qualified taxpayer. Amounts shall be treated as properly chargeable to capital account if under the qualified taxpayer's method of tax accounting they are properly includible in the qualified taxpayer's basis for computing depreciation on the qualified property under Revenue and Taxation Code Section 17250. However, any amounts not required to be included in the qualified taxpayer's basis for depreciation purposes shall not be treated as qualified costs. For example, Internal Revenue Code Section 179 provides that amounts for which an election is made under that section to currently deduct such amounts are "not chargeable to capital account." Thus, any amounts for which a qualified taxpayer makes an election to currently expense for California income or franchise tax purposes under either Internal Revenue Code Sections 179 or 179A, or amounts for which a qualified taxpayer makes an election for California purposes to currently expense under Internal Revenue Code Section 179-type provisions such as Revenue and Taxation Code Sections 17267.6 (Targeted Tax Area businesses), 17267.2 (Enterprise Zone businesses), or 17268 (Local Agency Military Base Recovery Area businesses), are treated as amounts that are not properly chargeable to capital account. In addition, any costs paid or incurred for property with a useful life of less than one year which may properly be expensed under Internal Revenue Code Section 162 would be treated as amounts not properly chargeable to capital account. Although costs that are not properly chargeable to capital account are not treated as qualified costs, the portion of the cost of any item of qualified property that is properly chargeable to capital account (such as, for example, the amount in excess of what may be currently deducted under Section 179 of the Internal Revenue Code) may be a qualified cost under Revenue and Taxation Code Section 17053.37.

EXAMPLE 1: F, a qualified taxpayer, purchases 50 stainless steel racks for \$900 from G for use in F's production line in Palmdale. F pays \$72 (\$900 X 8%) in California sales tax on the purchase. F makes an election for California franchise tax purposes to currently expense the entire cost of the stainless steel racks under Revenue and Taxation Code Section 17255 (Internal Revenue Code Section 179). Under these facts, the \$900 paid by F for the stainless steel racks would not be treated as a qualified cost since the \$900 is not properly chargeable to F's capital account under Revenue and Taxation Code Section 17255 (Internal Revenue Code Section 179).

EXAMPLE 2: H, a qualified taxpayer doing business in the Fresno Enterprise Zone, purchases a drill press for \$25 from I, and pays \$2 (8% of \$25) in California sales tax on the purchase. H makes an election under Revenue and Taxation Code Section 24356.7 to expense 40% of the cost of the drill press. Under these facts, \$10 of the \$25 paid by H would not be treated as a qualified cost since the \$10 is not properly chargeable to H's capital account.

(d) *Capitalized Labor Costs.* For costs paid or incurred by the qualified taxpayer for capitalized labor, the requirement that California sales or use tax be paid in order for the costs to be treated as qualified costs shall not apply. The qualified taxpayer shall have the burden of establishing the amount of any cost paid or incurred for capitalized labor that is a direct labor

cost, as that term is used in Section 263A of the Internal Revenue Code and defined in the regulations thereunder, that can be identified or associated with and are properly allocable to the construction, modification, or installation of any item of qualified property. This burden may, for example, ordinarily be satisfied by either an invoice, supported by the books and records of the qualified taxpayer, that separately states the amount of capitalized direct labor for qualified property acquired by purchase or, in the case of self-constructed qualified property, from books and records of the qualified taxpayer that establish the amount of capitalized direct labor for the construction of the item of qualified property.

EXAMPLE 1: G, a qualified taxpayer, purchases a machine that is qualified property from X for \$500. The price of the machine includes \$50 in separately stated shipping charges. X collects California sales tax of \$34 (8% of \$450) from G, with the shipping charges assumed to be exempt from California sales and use tax. Upon receipt of the machine, G incurs an additional \$50 in capitalized direct labor costs to have G's employees install the machine in G's manufacturing facility in Riverside, and \$25 in training costs to train G's personnel to properly operate the machine. Under these facts, only the cost of the machine upon which California sales tax was paid (\$450), plus the capitalized direct labor installation costs (\$50), would be treated as qualified costs. The \$50 paid for shipping charges is not a qualified cost since no California sales tax was paid on such amounts, nor are the shipping charges treated as capitalized direct labor costs. The \$25 incurred by G in training costs is not a qualified cost since training costs are indirect labor costs under subsection (a)(2) of Regulation 17053.37-2.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that the \$50 in freight charges are not separately stated and X collects \$40 (8% of \$500) in California sales tax from G. Under these facts, the cost of the machine, including the freight charges, upon which California sales tax was paid (\$500), plus the capitalized direct labor installation costs (\$50), would be treated as qualified costs.

EXAMPLE 3: J, a qualified taxpayer, purchases an extended warranty contract on qualified property. J's extended warranty contract provides that all unscheduled maintenance and repairs will be performed at no cost by the seller or its agent. Assume that the costs of the extended warranty contract are exempt from California sales and use tax. Under these facts, the extended warranty contract is not treated as a capitalized direct labor cost since it is not for the construction, modification, or installation of qualified property. As a result, the costs paid for the extended warranty contract are not qualified costs.

EXAMPLE 4: K, a qualified taxpayer, purchases a machine that is qualified property and then uses its own employees to install and modify the machine, including necessary adjustments, alignments and "debugging," so that the machine will properly run K's assembly line. Under these facts, assuming that K properly capitalizes for California tax purposes its direct labor costs for installing and modifying the machine, the labor costs are treated as capitalized direct labor costs and are thus qualified costs.

EXAMPLE 5: L, a qualified taxpayer, purchases a comprehensive insurance policy on an item of qualified property. L may not include the premiums for the insurance policy as qualified

costs because the insurance policy covers risk of loss, and is not a capitalized direct labor cost that is associated with the construction, modification or installation of qualified property.

(1) *Capitalized Labor Costs Under Third-Party Contracts.* Only capitalized direct labor costs, as that term is used in Section 263A of the Internal Revenue Code and defined in the regulations thereunder, that can be identified or associated with and are properly allocable to the construction, modification, or installation of specific items of qualified property, constitute qualified costs for purposes of the JSF Property Credit. For capitalized labor costs paid or incurred by a qualified taxpayer to a third-party contractor for the construction, modification or installation of qualified property, a qualified taxpayer is only allowed to include as qualified costs those direct labor costs that the qualified taxpayer could include if the qualified taxpayer had itself constructed the qualified property using its own employees. To determine whether the labor costs can be included as capitalized direct labor costs for the JSF Property Credit, the qualified taxpayer is required to look through its contract with the third party and put itself in the shoes of the third party for purposes of computing qualified costs.

EXAMPLE 1: H, a qualified taxpayer, contracts with I for \$100 to have a machine that is qualified property modified to increase its per-unit output. Assume that the labor costs associated with the modification are exempt from California sales and use tax. Assume also that \$45 of the \$100 contract constitutes direct labor costs paid by I to its employees under Section 263A of the Internal Revenue Code and the regulations thereunder. Although H does not pay California sales or use tax on the modification work, H may include in its qualified costs a portion of the costs of modifying the machine since \$45 of the \$100 is properly treated as a capitalized direct labor cost for the modification of qualified property. H must "look-through" the contract with I so that only those costs that constitute capitalized direct labor costs with respect to payments made by I to its employees shall constitute direct labor costs with respect to H.

(e) *Qualified Costs Paid or Incurred Pursuant to Binding Contracts.* For any qualified property constructed, reconstructed, or acquired by the qualified taxpayer (or any person related to the qualified taxpayer within the meaning of Internal Revenue Code Sections 267 or 707) pursuant to a binding contract in existence on or prior to January 1, 2001, costs paid pursuant to that contract shall be subject to allocation under the rules in this subsection.

(1) *Allocation of Costs Actually Paid Prior to January 1, 2001.* In any case where a qualified taxpayer has actually paid amounts (including, without limitation, contractual deposits and option payments) prior to January 1, 2001, under a binding contract, any such amounts shall not be treated as qualified costs. However, if under any binding contract a qualified taxpayer has paid amounts both before and after January 1, 2001, then the amounts actually paid after December 31, 2000, to the extent properly allocable to the construction, reconstruction, or acquisition of qualified property, shall be treated as qualified costs. In the case of any contract that was binding on January 1, 2001, under the terms of which a qualified taxpayer will acquire both qualified property and non-qualified property, and the qualified taxpayer has actually paid amounts both before and after January 1, 2001, then the amounts paid prior to January 1, 2001, and the amounts paid after December 31, 2000, must be allocated between the qualified property and the non-qualified property in proportion to the actual amounts paid prior to January 1, 2001, and the total contract price.

(2) *Binding Contract Bid Amount Reduced by Credit.* In no event shall the allocation provided in this subsection be allowed unless the bid that was the basis of the binding contract in existence on or prior to January 1, 2001, was reduced by the amount of the JSF Property Credit allowable as required by Revenue and Taxation Code Section 17053.37(i)(2) and Regulation 17053.37-7.

EXAMPLE 1: On October 1, 2000, M, a qualified taxpayer, executes a contract to purchase five machines and ten computers that are qualified property for a total of \$100 (plus applicable California sales tax). M will use the qualified property to complete a subcontract where the bid amount was reduced by the amount of the JSF Property Credit allowable. Under the terms of the contract, M is required to make a non-refundable \$20 deposit upon execution of the contract and pay the remaining \$80 upon delivery of the machines and computers. On May 1, 2001, the machines and computers are delivered and M pays the remaining \$80 due under the contract. Under these facts, the \$20 actually paid by M in 2000 will not be treated as a qualified cost, but the remaining \$80 paid in 2001 will be treated as a qualified cost.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that the computers are not qualified property because M intends to use them for general administrative purposes. The computers represent \$20 of the total \$100 contract price. Under these facts, since M is purchasing both qualified property and non-qualified property under a binding contract, the \$20 paid prior to January 1, 2001, and the \$80 paid after December 31, 2000, must be allocated between the machines and the computers. Since the cost of the machines represent 80% of the total contract price (\$80/\$100), and \$20 was actually paid prior to January 1, 2001, \$16 (80% of \$20) of the total \$80 paid for the machines is treated as having been paid prior to January 1, 2001, and is thus not treated as a qualified cost. However, the remaining \$64 (\$80 - \$16) paid for the machines is treated as a qualified cost.

EXAMPLE 3: Assume the same facts as in EXAMPLE 1, except that the qualified taxpayer did not reduce the amount of the bid that formed the basis of the subcontract by the amount of the JSF Property Credit allowable. Under these facts, M is not entitled to any credit since the bid amount was not reduced by the amount of the JSF Property Credit allowable.

(3) *Binding Contracts.* For purposes of Regulations 17053.37-1 through 17053.37-11, inclusive, a contract shall be treated as binding where the contract is enforceable under state law against the qualified taxpayer (or any related party within the meaning of Internal Revenue Code Sections 267 or 707) and the amount of potential damages (whether by an express liquidated damages provision or otherwise) for which the qualified taxpayer may be liable upon cancellation or breach of the contract would equal or exceed five percent (5%) of the total contract price. However, a contract to acquire a component part of a larger item of property shall only be treated as a binding contract to acquire such component part and shall not be treated as a binding contract to acquire the larger item of property under the general rule for binding contracts. For example, a written binding contract to acquire a motor to power a drill press would be a binding contract only for the motor, not for the entire drill press.

EXAMPLE 1: X, a qualified taxpayer, enters into a written contract with Y on August 15,

2000, under which X agrees to purchase 10 machines for \$150 for delivery on December 1, 2001. Under the terms of the contract, X is required to make a non-refundable deposit of \$10 upon execution of the contract. Under these facts, since X's potential damages upon cancellation or breach of the contract equal or exceed 5% of the total contract price (\$10/\$150, or 6.7%), X's contract with Y is treated as a binding contract in existence on or prior to January 1, 2001.

EXAMPLE 2: Assume the same facts as in *EXAMPLE 1*, except that Y is required to refund half of X's \$10 deposit in the event X cancels the contract. Assume further that X's potential damages to Y upon breach of the contract are limited by a liquidated damages provision to the \$5 of X's deposit that Y is not required to refund to X. Under these facts, X's contract is not treated as a binding contract in existence on or prior to January 1, 2001, since X's potential damages under the contract are less than 5% of the total contract price (\$5/\$150, or 3.3%).

(4) *Successor or Replacement Contracts.* Any contract entered into on or after January 1, 2001, that is a successor or replacement contract to a contract that was binding prior to January 1, 2001, shall be treated as a binding contract in existence prior to January 1, 2001, and shall be subject to the same rules described in this section applicable to binding contracts generally. However, if a successor or replacement contract is entered into on or after January 1, 2001, and the subject of the successor or replacement contract relates both to amounts to be paid or incurred for the construction, reconstruction, or acquisition of qualified property described in the original binding contract and to amounts to be paid or incurred for the construction, reconstruction, or acquisition of qualified property not described in the original binding contract, then the portion of those amounts described in the successor or replacement contract that were not described in the original binding contract shall not be treated as costs paid or incurred pursuant to a binding contract in existence prior to January 1, 2001.

EXAMPLE 1: On December 15, 2000, P, a qualified taxpayer, enters into a binding contract with Q to purchase three drill presses that are qualified property for a total contract price of \$50. Under the terms of the contract, P makes a non-refundable \$10 deposit to Q on December 20, 2000. On February 15, 2001, P and Q mutually agree to rescind the original contract and simultaneously execute a new contract under which P requests minor modifications to the specifications for the drill presses. Under the new contract, the total contract price is increased to \$55 to compensate Q for Q's additional costs of modifying the specifications for the drill presses. Under these facts, the February 15, 2001, contract is treated as a replacement contract to the December 15, 2000, contract, and the \$10 deposit made by P on December 20, 2000, is not treated as a qualified cost.

EXAMPLE 2: Assume the same facts as in *EXAMPLE 1*, except that upon rescission of the original contract Q refunds P's \$10 deposit. Under the terms of the new contract P is legally obligated to make a non-refundable deposit of \$15 to Q within 30 days of the execution of the contract. Under these facts, the new contract is still treated as a replacement contract. Despite Q's refund to P, \$10 of the total \$15 deposit made by P under the new contract is properly treated as having been actually paid prior to January 1, 2001, and will not be treated as a qualified cost.

EXAMPLE 3: Assume the same facts as in *EXAMPLE 1*, except that under the new contract P agrees to purchase five drill presses instead of the three drill presses under the original

contract. The total contract price for the new contract is increased to \$85. Under these facts, the new contract is still treated as a replacement contract with respect to the three drill presses which were the subject of the original contract, and the \$10 actually paid by P prior to January 1, 2001, is not treated as a qualified cost.

EXAMPLE 4: On November 1, 2000, R, a qualified taxpayer, enters into a binding contract with S to purchase two machines for \$10 each and five computers for \$2 each, for a total contract price of \$30. Assume that the machines are qualified property, but since R will use the computers in its general administrative office, the computers are not qualified property. Under the terms of the contract, R makes a non-refundable \$10 deposit to S on November 5, 2000. On March 1, 2001, R and S mutually agree to rescind the original contract and simultaneously execute a new contract under which R agrees to purchase three machines and five computers for \$40. Under these facts, the March 1, 2001, contract is treated as a replacement contract to the November 1, 2000, contract to the extent of the two machines and the five computers, but is not treated as a replacement contract as to the third machine added by the March 1, 2001, contract. The \$10 deposit actually paid prior to January 1, 2001, is not treated as a qualified cost. However, none of this \$10 deposit amount is required to be allocated to the third machine for purposes of allocating the total contract price between the qualified property and the non-qualified property because the March 1, 2001, contract is not treated as a binding contract under this section as to the third machine, so that the entire \$10 cost of the third machine is a qualified cost.

(5) *Option Contracts.* For purposes of Regulations 17053.37-1 through 17053.37-11, inclusive, in any case where a qualified taxpayer (or any related party within the meaning of Internal Revenue Code Sections 267 or 707) had an option to acquire qualified property on or prior to January 1, 2001, the option shall generally be treated as a binding contract. However, if the option holder would be required to forfeit an amount that is less than ten percent (10%) of the fixed option price upon cancellation or non-exercise of the option, then the option shall not be treated as a binding contract.

EXAMPLE 1: On May 1, 2000, F, a qualified taxpayer, pays \$150 to G for the right to purchase G's aluminum die-casting equipment for a total contract price of \$900 (including the amount paid for the option) at any time prior to May 1, 2002. Under the terms of the option, the \$150 is not refundable in the event F does not exercise its option. On January 15, 2002, F exercises its option to purchase G's casting equipment and delivers the remaining \$750 due to G under the terms of the option. Since the option holder would have been required to forfeit more than 10% of the fixed option price upon cancellation or non-exercise of the option ($\$150/\900 , or 17%), the option is treated as a binding contract and the \$150 paid by F prior to January 1, 2001, is not treated as a qualified cost.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that F pays only \$80 for the option and is not obligated to forfeit any additional monies to G in the event F chooses not to exercise the option. Under these facts, the option is not treated as a binding contract since the maximum amount that F would be required to forfeit under the option contract is less than 10% of the fixed option price ($\$80/\900 , or 9%).

(6) *Conditional Contracts.* A contract shall be treated as binding notwithstanding the fact

that the contract is subject to a condition.

EXAMPLE: On December 1, 2000, T, a qualified taxpayer, enters into a contract to purchase seven machines that are qualified property. The contract provides for a twenty percent (20%) down payment on December 1, 2000, with the balance to be paid on January 30, 2001. However, T's obligations under the contract are expressly conditioned upon the completion of T's new manufacturing facility in Palmdale. Despite this condition, the contract is treated as a binding contract in existence on or prior to January 1, 2001.

Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.

Regulation 17053.37-5

Qualified Property -- (See Regulation 17053.37-0 for Table of Contents.)

(a) *In General.* For purposes of Regulations 17053.37-1 through 17053.37-11, inclusive, the term "qualified property" includes tangible personal property, whether new or used, that is defined in Internal Revenue Code Section 1245(a)(3)(A) and is used by a qualified taxpayer primarily in qualified activities to manufacture a product for ultimate use in a Joint Strike Fighter. The term "qualified property" does not include certain types of property described in subsection (c) of this regulation. The basis of any qualified property for which the JSF Property Credit is claimed is not required to be reduced by the amount of any JSF Property Credit claimed.

(b) *General Requirements for Qualified Property.* In order for property to be treated as qualified property, the property must satisfy each of the requirements of this subsection of this regulation.

(1) *Tangible Personal Property.* For purposes of this section, property must be tangible personal property. The term "tangible personal property" means any tangible property except land and improvements thereto, such as buildings or other inherently permanent structures (including items which are structural components of such buildings or structures). Tangible personal property includes all property (other than structural components) which is contained in or attached to a building. Thus, for example, production machinery, printing presses, and testing equipment which is contained in or attached to a building are tangible personal property. Furthermore, all property which is in the nature of machinery (other than structural components of a building or other inherently permanent structures) shall be considered tangible personal property even though located outside a building. The determination of whether property will be treated as an inherently permanent structure shall be made under Internal Revenue Code Section 1245(a), so that generally property will be treated as an inherently permanent structure (and thus not tangible personal property) if the property is either intended to be or is in fact affixed permanently, and is either incapable of being moved or, if movable, would suffer a significant degree of damage upon its removal. Local law, including state, county, city, or regional, shall not be controlling for purposes of determining whether property is or is not "tangible" or "personal,"

so that the fact that under local law property is held to be personal property or tangible property shall not affect the determination of whether such property is tangible personal property for purposes of the JSF Property Credit.

EXAMPLE 1: B, a qualified taxpayer, manufactures aircraft engines in a manufacturing plant located in Tustin. B decides to upgrade its assembly line by installing a heavy-duty overhead crane which will be permanently affixed to the building structure. Prior to installing the crane B constructs steel columns that extend from the crane's girder to the roof of the building. Under these facts, while the steel columns may be treated as "other tangible property" under Internal Revenue Code Section 1245(a)(3)(B), the steel columns are not tangible personal property and thus are not qualified property.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except instead consider the heavy-duty overhead crane. The crane moves back and forth along the assembly line on craneway tracks that are permanently bolted to the building's ceiling beams and is hard-wired to the building's electrical system. Despite its permanent affixation to the building, the crane is an item of tangible personal property.

(2) *Section 1245(a)(3)(A) Property.* Only personal property described in Internal Revenue Code Section 1245(a)(3)(A) is treated as qualified property for purposes of the JSF Property Credit. Other tangible property that is described in Internal Revenue Code Sections 1245(a)(3)(B) through (F) is not "personal" property and is thus not qualified property under Revenue and Taxation Code Section 17053.37.

EXAMPLE 1: F, a qualified taxpayer, manufactures airplane fuselages. F constructs a building which is open at both ends through which a length of track travels to move the fuselages during several steps in the manufacturing process. Since the building is not tangible personal property defined in Internal Revenue Code Section 1245(a)(3)(A), it would not be treated as qualified property.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, but in addition, F constructs and installs machinery in the building to facilitate the assembly of the fuselages. Although the machinery is permanently installed in the building, it is not a structural component of the building and can be removed without dismantling the building. As a result, the machinery is tangible personal property that is defined in Internal Revenue Code Section 1245(a)(3)(A).

(3) *Used to Manufacture a Product for Ultimate Use in a Joint Strike Fighter.* Property must be used in qualified activities to manufacture a product for ultimate use in a Joint Strike Fighter. This requirement will be satisfied if the qualified taxpayer is using the qualified property primarily to manufacture a product that is properly treated as inventory of the qualified taxpayer and that is physically installed in or attached to a Joint Strike Fighter aircraft. For this purpose, the term "inventory" includes any property that is required to be included in the qualified taxpayer's inventory under Internal Revenue Code Section 263A or that is described in Internal Revenue Code Section 1221(1).

EXAMPLE 1: B, a qualified taxpayer, manufactures aircraft radar antennas that are attached to a Joint Strike Fighter. B constructs a compressor for use in B's assembly line. B uses the compressor exclusively to manufacture the antennas. Since B uses the compressor to manufacture a product that is physically attached to a Joint Strike Fighter aircraft, the compressor is primarily used in a qualified activity.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except B manufactures ground based radar equipment to be used in connection with the Joint Strike Fighter program. Under these facts, even though the radar equipment is being manufactured in connection with the Joint Strike Fighter program, the compressor is not used in qualified activities since the compressor is used to manufacture a product that is not physically attached to a Joint Strike Fighter aircraft.

(4) *Primarily Used in Qualified Activities.* Property must be primarily used in qualified activities.

EXAMPLE 1: B, a qualified taxpayer, manufactures avionics systems in San Diego. B constructs a compressor for use in B's assembly line. The compressor is used for 500 hours in the assembly line, which is part of B's qualified activities, and for 250 hours in B's warehouse, which is part of B's non-qualified activity. Since B used the compressor in B's qualified activities for more than 50 percent of the time the compressor was actually in use during the 12-month period following the date the compressor was placed in service in California by B (500 hours/750 hours, or 66.7%), the compressor is primarily used in a qualified activity.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except B instead uses the compressor for 500 hours in the non-qualified activity and 250 hours in the qualified activity. Under these facts, the compressor is not primarily used in a qualified activity since the compressor was used less than 50 percent of the time during the 12-month period following the date the compressor was placed in service in California by B in a qualified activity (250 hours/750 hours, or 33.3%).

EXAMPLE 3: Assume the same facts as in EXAMPLE 1, except B uses the compressor for a total of 100 days during the 12-month period following the date the compressor was placed in service in California by B. During each of those 100 days, B uses the compressor for four hours in the qualified activity and six hours in the non-qualified activity. Although B is using the compressor in the qualified activity during each of the 100 days that it is actually in operation, the compressor is not primarily used in a qualified activity because the total number of hours the compressor is used in a qualified activity is less than 50 percent of the total hours of operation of the compressor during the 12-month period following the date the compressor was placed in service in California by B.

EXAMPLE 4: C, a qualified taxpayer, manufactures aircraft communications equipment in San Jose. C purchases ten personal computers to be used in the company offices. The computers are to be used in part for administration and management, a non-qualified activity, but are also used for the tracking of assembly line operations by directly monitoring the performance, safety, and production of the assembly line, a qualified activity. As long as the computers are used at least 50 percent of the time in the qualified activity during the 12-month period following the

date the compressor was placed in service in California by C, then C shall be treated as primarily using the computers in a qualified activity.

EXAMPLE 5: R, a qualified taxpayer, manufactures aircraft instrument lights from raw materials such as glass, tungsten, aluminum, copper and paper. R initially receives the raw materials at its warehouse in North Hollywood, and then, when needed, transports them using its own trucks to R's manufacturing plant in Burbank. Upon delivery to the manufacturing plant, the raw materials are placed in a receiving area where they are then moved via forklift to their respective areas in the plant for introduction into the process of manufacturing the light bulbs. Under these facts, R's qualified property does not include the trucks used to transport the raw materials from the warehouse to the manufacturing plant since the raw materials have not been introduced into R's manufacturing "process" until the raw materials have been delivered to the manufacturing plant. However, the forklift would be qualified property (assuming it was not used more than 50 percent of the time to unload the raw material from the trucks to the receiving area) since once the raw materials are received at the same premises where R's manufacturing activity is being conducted, the movement of the raw materials via forklift is treated as part of R's manufacturing process.

EXAMPLE 6: T, a qualified taxpayer, manufactures copper wire in Santa Ana. As part of T's manufacturing process, T purchases a machine to process the copper wire by coating it with white or black insulation prior to wrapping the wire in white plastic insulation. T's machine applies the materials and labor necessary to modify or change the characteristics of the copper wire. T's machine is used in "processing" the wire and thus would be qualified property.

EXAMPLE 7: Assume the same facts as in EXAMPLE 7, except that T also uses the machine to coat its mailing labels for shipment of the wire. Assume that the processing of the copper wire is complete upon its being wrapped in the plastic insulation, and that the number of hours the machine is used during the 12-month period following the date the machine was placed in service in California by T for the "processing" of the wire is less than 50 percent of the machine's total use during such period. Under these facts, the machine is no longer primarily used for "processing," a qualified activity, but is instead primarily used to coat the mailing labels, a non-qualified activity, so that the machine is not qualified property.

EXAMPLE 8: C, a qualified taxpayer, manufactures hydraulic lines in Milpitas. The employees of C fabricate and assemble shelving to be used to store the manufactured lines following completion of C's manufacturing process. Assume that the costs of fabricating the shelving, including the direct labor costs, are properly capitalized by C. Although C has "fabricated" the shelving, the shelving is not qualified property since it is not used in C's manufacturing process, which is a qualified activity, but is rather used for storage, which is a non-qualified activity.

EXAMPLE 9: C, a qualified taxpayer, manufactures ground based radar equipment and radar equipment that is physically installed in or attached to a Joint Strike Fighter aircraft. C purchases a compressor to use on its assembly line. The compressor is used for a total of 500 hours on the assembly line, 300 hours to manufacture the radar equipment that is physically installed in or attached to a Joint Strike Fighter aircraft and 200 hours to manufacture the ground

based equipment. Since B used the compressor in B's qualified activities for more than 50 percent of the time the compressor was actually in use during the 12-month period following the date the compressor was placed in service in California by B (300 hours/500 hours, or 60%), the compressor is primarily used in a qualified activity.

EXAMPLE 10: Assume the same facts as in EXAMPLE 10, except the compressor is used 200 hours to manufacture the radar equipment that is physically installed in or attached to a Joint Strike Fighter aircraft and 300 hours to manufacture the ground based equipment. Since B used the compressor in B's qualified activities for less than 50 percent of the time the compressor was actually in use during the 12-month period following the date the compressor was placed in service in California by B (200 hours/500 hours, or 40%), the compressor is not primarily used in a qualified activity.

(c) *Specifically Excluded Property.* Notwithstanding subsections (b) or (d) of this regulation, qualified property does not include any of the following:

(1) *Furniture.* Any item of furniture, regardless of how used or where located.

(2) *Facilities Used for Warehousing Purposes.* Any property used for warehousing purposes after completion of the manufacturing process. Thus, for example, a manufacturer of engine components that stores its finished products in a separate warehouse building prior to shipment, and thereafter uses forklifts and other heavy equipment to move the inventory within the warehouse building, shall not treat the forklifts and other heavy equipment as qualified property.

(3) *Inventory.* Any property that is properly treated as inventory of the qualified taxpayer. For this purpose, the term "inventory" includes any property which is required to be included in the qualified taxpayer's inventory under Internal Revenue Code Section 263A or that is described in Internal Revenue Code Section 1221(1).

(4) *Equipment Used to Store Finished Products.* Any equipment used to store finished products that have completed the manufacturing process. Thus, for example, if a qualified taxpayer primarily uses a forklift in the finished goods portion of its manufacturing plant to transport finished products to its loading dock for shipping to customers, the forklift would not be qualified property. On the other hand, if the forklift was primarily used to transport raw materials to the assembly line and was occasionally used to transport finished products to the loading dock for shipment to customers, the forklift would be treated as qualified property.

(5) *Tangible Personal Property Used in Administration, General Management, or Marketing.* Any tangible personal property that is used in administration, general management, or marketing. For this purpose, an item of property that is used both in a qualified activity and for administration, general management, or marketing, shall be treated as qualified property only if the item is primarily used in a qualified activity. However, property primarily used to clean and maintain the factory floor and fire safety equipment primarily used on the factory floor are not considered tangible personal property used in administration, general management, or marketing.

(d) *Movement of Used Property Into This State.* In any case where property is moved from

another state or country into this state by a qualified taxpayer or by a lessor who intends to lease such property to a qualified taxpayer, the property may generally be treated as qualified property for purposes of the JSF Property Credit if it satisfies the other requirements of this regulation. Thus, for example, if an item of property is acquired and placed in service in Nevada in 2000, and thereafter the item of property is moved into this state for use in a qualified activity (as defined in Regulation 17053.37-5(b)), the property may generally be treated as qualified property. However, in the case of any such moved property, a qualified taxpayer or lessor must still satisfy the requirements of Regulation 17053.37-4 (relating to qualified costs and payment of California sales or use tax) in order to claim the JSF Property Credit.

Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.

Regulation 17053.37-6

Leasing -- (See Regulation 17053.37-0 for Table of Contents.)

(a) *In General.* For purposes of Regulations 17053.37-1 through 17053.37-11, inclusive, in the case of any leasing transaction in which qualified property is leased by a qualified taxpayer, the rules of this regulation shall apply. Generally, the lessor must pay California sales tax on the lessor's acquisition of the qualified property in order for the lessee to claim the credit for that item of qualified property. Conversely, the lessee cannot claim the JSF Property Credit for an item of property where the lessor acquired the qualified property without paying California sales or use tax and the lessor instead collects use tax payments from the lessee measured by the lessee's rental payments to the lessor. The determination of whether the rules in subsection (b) or subsection (c) of this regulation apply shall be made by reference to the sales and use tax treatment of the lease, rather than the income tax treatment of the lease. Thus, for example, a lease of qualified property that would be treated as a finance lease under income tax principles may still be treated as an operating lease under this regulation. In addition, under California sales and use tax law, a transaction denominated as a lease will instead generally be treated as a sale under a security agreement if the lease contains a nominal option price. For this purpose, California sales and use tax law generally treats the option price as nominal if it does not exceed the lesser of \$100 or 1 percent of the total contract price.

EXAMPLE 1: X, a leasing company, agrees to lease qualified property to Y, a qualified taxpayer, for use in Y's manufacturing facility in Garden Grove. Under the terms of the lease, X will lease the property to Y for \$100 per year for a term of 10 years. Upon the expiration of the 10-year lease term, Y has an option to acquire the property for \$1. Under these facts, the "lease" would be properly treated as a sale under a security agreement from its inception and not as a lease under Revenue and Taxation Code Section 6006.3 and California State Board of Equalization Regulation 1660(a)(2)(A), Title 18, California Code of Regulations, so that the rules of subsection (c) of this regulation would apply.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that Y's option price is \$125, or 12.5% of the total contract price. Under these facts, notwithstanding that the "lease"

may be treated as a finance lease (and thus as a "purchase") for California franchise and income tax purposes, under California sales and use tax law the "lease" would generally be treated as a lease and the rules of subsection (b) of this regulation would apply.

(1) *Lessor Not Entitled to JSF Property Credit.* A lessor of qualified property is never entitled to claim the JSF Property Credit with respect to any item of qualified property it leases to another party, regardless of whether the lessor is otherwise a qualified taxpayer.

(2) *Binding Contract Rules Applicable to Leases.* In the case of any qualified property leased pursuant to any agreement or contract that is treated as a binding contract under the rules of subsection (e) of Regulation 17053.37-4, the allocation rules of subsection (e) of Regulation 17053.37-4 shall apply in determining the amount of the qualified cost to the lessor upon which the lessee is entitled to claim the JSF Property Credit. For this purpose, if a lessor acquires qualified property under the terms of a contract that is treated as a binding contract with respect to the lessee (or a party related to the lessee within the meaning of Internal Revenue Code Sections 267 or 318), then any payments or reimbursements made by the lessor, directly or indirectly in the form of a reduction in the amount of lease rental payments to be paid by the lessee under the lease, upon or as a result of the lessor's assumption of the lessee's obligations under the binding contract, shall be treated in the same manner as if the lessor had not assumed the lessee's obligations under the contract. Finally, in any case where a lessor has acquired property prior to January 1, 2001, and thereafter leases such property, the qualified cost to the lessor upon which the lessee would be entitled to claim the JSF Property Credit would generally be zero (assuming the lessor has not paid otherwise qualified costs after January 1, 2001, to improve or otherwise modify the leased property, in which case the lessor would have qualified costs to the limited extent of such post-2000 amounts that were paid).

EXAMPLE 1: D, a qualified taxpayer, is engaged in the business of manufacturing aircraft landing gear in Palmdale. On September 20, 2000, D enters into a contract with X to acquire 3 machines that are qualified property for a total contract price of \$900. Under the terms of the contract, D makes a non-refundable deposit to X of \$150 upon execution of the contract, with an additional \$150 due on July 1, 2001, and the final payment of \$600 payable upon delivery of the machines on February 15, 2002. Assume that this contract is treated as a binding contract under subsection (e) of Regulation 17053.37-4. On January 15, 2002, D decides that it would prefer to instead lease the machines, so D enters into a contract with L, an equipment leasing company, under which L will (i) assume D's obligations under D's contract with X, (ii) lease the qualified property to D for a term of 10 years, and (iii) refund to D the \$300 in payments that D has previously made to X. Assume that L will pay California sales tax on its purchase of the qualified property from X. Under these facts, L will be treated as having \$750 in qualified costs for which D will be entitled to claim the JSF Property Credit, which is the total amount treated as paid by L after January 1, 2001 (\$600 paid directly by L to X under X's contract with D, plus \$150 paid by L to D as reimbursement for D's payment on July 1, 2001, but excluding the \$150 paid by D to X prior to January 1, 2001).

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that instead of L agreeing to refund the \$300 in payments that D has previously made to X, L instead reduces the amount of the rental payments to be due from D under the lease. Under these facts, the result is the same as

in EXAMPLE 1.

(3) Special Rules Applicable to All Leasing Transactions

A. Placed in Service In the case of any leasing transaction, the requirement that qualified property must be placed in service in California in order for a qualified taxpayer to claim the JSF Property Credit shall be treated as having been satisfied at the time when all the terms and conditions of the lease contract have been completed so that the lessee has an unconditional obligation to pay all rents due under the contract to the lessor of the qualified property. However, notwithstanding the preceding sentence, the requirement of subsection (b)(4) of Regulation 17053.37-5 that property be primarily used in qualified activities to manufacture a product for ultimate use in a Joint Strike Fighter must still be satisfied in order for a lessee to claim the JSF Property Credit.

B. Bid Amount Reduced by Credit. In no event shall any leasing transaction qualify for the JSF Property Credit unless the bid reduction requirements contained in Revenue and Taxation Code Section 17053.37(i)(2) and Regulation 17053.37-7 have been satisfied with respect to the bid which contains the Joint Strike Fighter Property Credit allowable for the qualified property that is the subject of the lease.

EXAMPLE: On July 1, 2001, A, a qualified taxpayer, enters into a contract to lease a drill press from B, an equipment leasing company, for use in A's manufacturing facility in Roseville. Under the terms of the lease contract, A's rental obligations commence at the beginning of the month following the date that A provides B with a written statement that the drill press has been received from C, the original manufacturer of the drill press, and that the drill press has been installed and is in good working order (e.g., A provides a Certificate of Acceptance to B). On January 15, 2002, A executes and delivers the required written statement to B. Under these facts, A is treated as having satisfied the "placed in service" requirement as of February 1, 2002, and, assuming all other requirements of Revenue and Taxation Code Section 17053.37 have been satisfied, A is entitled to claim the JSF Property Credit.

(b) Operating Leases. In the case of any lease that is not treated as a sale under Part 1 (commencing with Section 6001) of Division 2 of the Revenue and Taxation Code (relating to the payment and collection of California sales and use tax), the rules set forth in this subsection of this regulation shall apply. Any lease subject to the rules of this subsection of this regulation shall be referred to in this regulation as an "operating lease."

(1) In General. Under Revenue and Taxation Code Section 6006(g)(5), a lease of tangible personal property is generally treated as a sale for California sales and use tax purposes, unless the tangible personal property is leased in substantially the same form as acquired by the lessor or leased in substantially the same form as acquired by the transferor and the lessor or transferor has paid sales tax reimbursement or has paid use tax measured by the purchase price of the property.

EXAMPLE: L, a taxpayer engaged in the equipment leasing business, purchases 20 machine tools for \$10 from P, a retailer of machine tools. L intends to immediately lease the machine tools, without modification, to X, a qualified taxpayer engaged in the business of manufacturing

aircraft cockpit canopies in Visalia, for a term of 10 years. L pays California sales tax on its purchase of the machine tools, and then leases the machine tools to X. Assume that X does not have an option to purchase the machine tools upon the expiration of the lease term. Since L has paid California sales tax on its purchase of the machine tools and then leased the property in substantially the same form as acquired, L's lease to X is not treated as a sale under Revenue and Taxation Code Section 6006(g)(5) and the rules of this subsection of this regulation apply.

(2) *Applicable Requirements.* In the case of an operating lease, the following requirements must be satisfied in order for the lessee to claim the JSF Property Credit.

A. *Lessee Must Be a Qualified Taxpayer.* The requirement under Regulation 17053.37-3 that the user of the qualified property must be a qualified taxpayer shall be applied to the lessee and not to the lessor.

B. *Use of Property in Qualified Activities.* The requirement under subsection (b)(4) of Regulation 17053.37-5 that property be used in qualified activities in order to be treated as qualified property shall be applied to the lessee and not the lessor with respect to the property that is the subject of an operating lease.

C. *Sales or Use Tax Payment Requirement.* Except as provided in subsections (b)(3)(B) or (b)(5)(B) of this regulation (relating to capitalized labor), the lessor must pay California sales tax reimbursement or California use tax on the lessor's construction, reconstruction or acquisition of the qualified property. In any case where the lessor's acquisition of the qualified property is pursuant to a transaction treated as either an occasional sale under Revenue and Taxation Code Section 6006.5 or as a sale of mobile transportation equipment (as defined in Revenue and Taxation Code Section 6023), the requirement of this subsection of this regulation shall be satisfied only if the lessor makes a timely election under either Revenue and Taxation Code Section 6094.1 or 6244(d) and pays California sales tax reimbursement or California use tax with respect to the lessor's acquisition of the qualified property.

D. *Qualified Costs.* The requirement that costs, in order to be treated as qualified costs, must be paid or incurred for the "construction, reconstruction, or acquisition" of qualified property shall not apply to the lessee's lease rental payments. Thus, for example, although a lessee may, under the lessee's method of California tax accounting, currently deduct its lease rental payments, the lessee will still be entitled to claim the JSF Property Credit if the other requirements of this subsection of this regulation are satisfied. However, the rules of Regulation 17053.37-4, including the rules relating to the allocation of costs paid or incurred pursuant to binding contracts, shall apply in determining the amount of qualified costs of the lessor upon which the lessee may determine its JSF Property Credit.

E. *Chargeable to Capital Account.* The requirement that costs, in order to be treated as qualified costs, must be properly chargeable to the capital account of the qualified taxpayer shall not apply to the lessee's lease rental payments. Thus, for example, although a lessee may, under the lessee's method of California tax accounting, currently deduct lease rental payments, the lessee will still be entitled to claim the JSF Property Credit if the other requirements of this subsection are satisfied.

(3) *Amount of JSF Property Credit Lessee May Claim.* In general, a lessee under an operating lease is entitled to claim the JSF Property Credit at the same time and in the same amount as if such lessee had instead constructed, reconstructed, or acquired the qualified property other than by lease.

A. *Qualified Cost to Lessor.* Except as provided in subsection (b)(3)(B) of this regulation, the qualified cost to the lessor upon which the lessee is entitled to claim the JSF Property Credit is generally equal to the purchase price amount on which California sales tax reimbursement or use tax has been paid by the lessor. Thus, for example, if a lessor pays \$100 for an item of qualified property, plus \$8 in California sales tax reimbursement on such item, the qualified cost to the lessor would be \$100.

B. *Exception For Capitalized Labor.* The qualified cost to the lessor under subsection (b)(3)(A) of this regulation shall also include any capitalized labor that is a direct cost, as that term is used in Section 263A of the Internal Revenue Code and defined in the regulations thereunder, that can be identified or associated with and are properly allocable to the construction or modification of the qualified property. Thus, for example, assume a lessor pays \$100 for an item of qualified property, with \$20 of a \$50 total labor cost properly treated as capitalized direct labor costs that are exempt from California sales or use tax. While the lessor would pay only \$4 (8% of \$50) in California sales tax reimbursement on the lessor's purchase of the qualified property, the qualified cost to the lessor under this subsection of this regulation would be equal to \$70 (\$50 + \$20).

(4) *Special Rules for Operating Leases.* The following special rules apply to any lease that is treated as an operating lease under this regulation.

A. *Limitation on Qualified Costs.* In determining a lessor's qualified cost under the rules of this subsection of this regulation, the allocation rule specified in Regulation 17053.37-4 shall apply to any costs actually paid by the lessor (or treated as paid by the lessor under the rules in this regulation) pursuant to a contract that was binding on January 1, 2001. Thus, for example, if a lessor has a binding contract to acquire qualified property for \$100 as of January 1, 2001, and has paid a non-refundable deposit of \$20 prior to January 1, 2001, and thereafter pays the remaining \$80 purchase price, the lessor's qualified cost upon which a lessee may claim the JSF Property Credit could not exceed \$80 (\$100 purchase price less \$20 actually paid prior to January 1, 2001, pursuant to a binding contract).

B. *Reduction in Qualified Cost to Lessor.* In the case of any re-lease of qualified property by a lessor to another qualified taxpayer, the qualified cost to the lessor under subsection (b)(3)(A) of this regulation as to the subsequent lessee shall first be reduced by the amount of qualified cost taken into account by any predecessor lessee. However, the preceding sentence shall not apply to the extent that the predecessor lessee was required to recapture any JSF Property Credit allowed to the predecessor lessee under the recapture rules in Regulation 17053.37-8.

EXAMPLE 1: L, a taxpayer engaged in the equipment leasing business, acquires two cranes from R, a manufacturer of cranes in Oxnard, for \$100. L intends to immediately lease the cranes

to M, a qualified taxpayer, for use by M in its manufacturing facility located in Ventura. Assume the lease is properly treated as an operating lease under this regulation and that L pays sales tax to R of \$8 (8% of \$100) at the time of L's purchase. Under these facts, M will be entitled to claim a \$10 JSF Property Credit (10% of \$100) since L's qualified cost is \$100.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that at the end of the lease term L re-leases the cranes to P, a qualified taxpayer, which manufactures synthetic resins and composite materials at a facility in Moorpark. Under subsections (b)(3)(A) and (b)(4)(B) of this regulation, L's qualified cost upon which P may claim the JSF Property Credit is zero (\$0) since L's qualified cost is \$0 (\$100 original qualified cost to L, less \$100 qualified cost taken into account by a predecessor lessee, M, when claiming the JSF Property Credit).

EXAMPLE 3: Assume the same facts as in EXAMPLE 2, except that M, the initial lessee, cancels the lease with L after 10 months, with L repossessing the cranes. Under these facts, M would be required to recapture (pursuant to Regulation 17053.37-8) the entire \$10 JSF Property Credit previously claimed by M, and L's qualified cost upon L's re-lease of the cranes to P would be \$100 (\$100 original qualified cost to L, less \$100 qualified cost taken into account by a predecessor lessee, M, plus \$100 of qualified cost recaptured upon M's cancellation of the lease with L).

C. Qualified Cost to Successor Lessor. In any case where a successor lessor acquires qualified property from a lessor that is subject to a lease (including any qualified property that is not currently being leased but which the successor lessor intends to re-lease) in a transaction that is not treated as a sale for California sales and use tax purposes, the qualified cost to the successor lessor for purposes of the JSF Property Credit shall be reduced by the amount of qualified cost of the predecessor lessor that was taken into account by any lessee in computing a credit under the JSF Property Credit. However, the preceding sentence does not apply in any case where the transaction in which the successor lessor acquires the qualified property from the predecessor lessor is treated as a sale for California sales and use tax purposes.

EXAMPLE 1: G is engaged in the equipment leasing business. G acquires three drill presses from Q, a manufacturer of drill presses, for \$300. G immediately leases the printing presses to D, a qualified taxpayer, for use by D in D's machine tool facility in Santa Barbara. Assume the lease is properly treated as an operating lease under this regulation, and that G pays sales tax to Q of \$24 (\$300 X 8%) at the time of purchase. Under these facts, D would be entitled to claim a JSF Property Credit of \$30 (10% of \$300, G's qualified cost of the drill presses). Three years later G sells the drill presses to H, who is also engaged in the business of equipment leasing, for \$250. Assume that G terminates its lease with D prior to the sale of the drill presses to H, and that H delivers a resale certificate to G so that H's purchase is exempt from California sales and use tax. Assume further that D agrees to re-lease the drill presses from H following H's acquisition of the drill presses from G. D terminates its lease two years after H's purchase of the drill presses, and H then re-leases the drill presses to E in a transaction treated as an operating lease under this regulation, for use by E in its tool and die facility in Bakersfield. Under these facts, H's qualified cost upon which E may claim the JSF Property Credit is \$0 (\$250 paid by H to G, less \$300 qualified cost taken into account by a predecessor lessee, D).

EXAMPLE 2: Assume the same facts as in *EXAMPLE 1*, except that G does not terminate its lease with D prior to G's sale of the drill presses to H. Under California sales and use tax law, the sale by G to H would be subject to California sales tax and H would not be entitled to deliver a resale certificate to G. As a result, assume H pays California sales tax reimbursement to G on the \$250 purchase price. Since H has paid California sales tax reimbursement to G, H's qualified cost upon which E may claim the JSF Property Credit is \$250.

D. Acquisition by Lessee of Leased Property. In any case where a lessee (or any party related to the lessee within the meaning of Internal Revenue Code Sections 267 or 318) of qualified property acquires the leased property from the lessor within one year of the date the qualified property is first used by the lessee, then the purchase of the qualified property by the lessee shall be treated as a disposition of the property by the lessee and any JSF Property Credit claimed by the lessee must be recaptured by the lessee under the rules of Regulation 17053.37-8. However, if the lessee (or related party) pays California sales or use tax on the acquisition of the qualified property, then the rules of Regulation 17053.37-4 shall apply to the acquisition and the lessee-purchaser may be entitled to claim the JSF Property Credit with respect to its costs of acquisition.

EXAMPLE 1: J, a qualified taxpayer, leases five lathes which are qualified property from Z, which is engaged in the equipment leasing business, for use in J's manufacturing facility in Folsom. Assume J's lease is treated as an operating lease under this regulation, and that J has claimed the JSF Property Credit. Nine months after J first uses the lathes, J exercises an option under the lease to acquire the lathes from Z for their fair market value. Under the rules of this regulation, and Regulation 17053.37-8, J would be required to recapture any JSF Property Credit claimed by J. However, if J paid California sales or use tax on the purchase of the lathes, then J may have qualified costs on J's purchase from Z under the rules of Regulation 17053.37-4.

EXAMPLE 2: Assume the same facts as in *EXAMPLE 1*, except that K, a wholly owned subsidiary of J, instead purchases the lathes from Z. Under the rules of this regulation, since K is related to J under both Internal Revenue Code Sections 267 and 318, K's acquisition of the lathes will be treated as a disposition by J of the qualified property and J will be required to recapture the JSF Property Credit. If K continues to lease the lathes to J, then the rules of subsection (b)(4)(C) of this regulation shall apply in determining whether K will have qualified cost in the lathes upon which J may claim a JSF Property Credit upon K's acquisition of the lathes. On the other hand, if K cancels the lease with J (assuming K may legally do so) and uses the lathes in a qualified activity conducted by K, then, assuming K has paid California sales or use tax on its acquisition, K may have qualified costs under the rules of Regulation 17053.37-4 assuming K continues to use the lathes in a qualified activity instead of re-leasing the lathes.

(5) Sale-Leaseback Transactions. In the case of any sale-leaseback transaction, the following rules shall apply:

A. General Rule. Except as provided in subsection (b)(5)(B) of this regulation, in the case of any sale-leaseback transaction in which a lessor does not pay California sales or use tax upon acquisition of an item of qualified property, the qualified cost to the lessor upon which the lessee would be entitled to claim the JSF Property Credit shall be zero.

EXAMPLE: On January 15, 2001, F, a qualified taxpayer engaged in the business of manufacturing aircraft navigational instruments, purchases three glass grinders that are qualified property from Y, the manufacturer of the glass grinders. Y collects California sales tax on the purchase by F. On January 30, 2001, F places the three grinders in service in its manufacturing facility in Crescent City. On May 15, 2001, G, which is engaged in the equipment leasing business, purchases the three grinders from F and immediately leases them back to F. Under the rules of this regulation, and Regulation 17053.37-8, F would be required to recapture any JSF Property Credit claimed by F. In addition, since this transaction would not be treated as an "acquisition sale and leaseback" under Revenue and Taxation Code Section 6010.65, G must pay California sales or use tax on G's purchase of the grinders in order for F to claim any JSF Property Credit under the rules of this regulation. If G delivers a resale certificate upon its acquisition of the grinders, so that G does not pay California sales or use tax upon G's acquisition of the grinders, then no JSF Property Credit could be claimed by F upon F's lease of the grinders from G.

B. Acquisition Sale and Leaseback. In the case of any transaction that is properly treated as an "acquisition sale and leaseback" under Revenue and Taxation Code Section 6010.65, the requirement of subsection (b)(2)(C) of this regulation (relating to payment of California sales or use tax) shall be deemed satisfied by the lessor. If a transaction is treated as an "acquisition sale and leaseback" under this subsection of this regulation, then the qualified cost to the lessor under subsection (b)(3)(A) of this regulation shall be equal to the amount upon which the lessee paid California sales or use tax, plus any capitalized labor costs determined under subsection (b)(3)(B) of this regulation. However, the rules of this subsection of this regulation shall only apply if, and to the extent that, the costs originally incurred by the lessee to acquire, construct, or reconstruct the qualified property were treated as qualified costs under Regulation 17053.37-4.

EXAMPLE 1: On December 1, 2001, P, a calendar year qualified taxpayer engaged in the business of manufacturing composite material, purchases and immediately places in service two mixing tanks that are qualified property from Z, the manufacturer of the mixing tanks. Z collects sales tax on the purchase by P. On January 15, 2002, R, which is engaged in the equipment leasing business, purchases the two mixing tanks from P and immediately leases them back to P. Since R's acquisition and leaseback occurs within 90 days of P's first functional use of the mixing tanks, and assuming the other requirements of Revenue and Taxation Code Section 6010.65 are satisfied, P's sale to R and R's leaseback to P are treated as an "acquisition sale and leaseback" under Revenue and Taxation Code Section 6010.65 and the rules of subsection (b)(5)(B) of this regulation would apply. Under the rules of this regulation, and Regulation 17053.37-8, P would be required to recapture any JSF Property Credit claimed on P's 2001 California return. However, R would be "deemed" to have paid California sales or use tax upon R's acquisition of the mixing tanks from P, and P would be entitled to claim an JSF Property Credit on its 2002 California return in an amount equal to R's qualified cost, as determined under subsections (b)(3)(A) and (b)(3)(B) of this regulation. For this purpose, R's qualified cost could not exceed P's qualified cost determined under Regulation 17053.37-4.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that P purchases and places the mixing tanks in service on December 1, 2000, and R purchases the mixing tanks from P and

immediately leases them back to P on January 15, 2001. Under these facts, even though the transaction would be treated as an "acquisition sale and leaseback" under Revenue and Taxation Code Section 6010.65, since P's qualified cost under Regulation 17053.37-4 would be equal to zero, R's qualified cost under this regulation would similarly be equal to zero, and thus no JSF Property Credit would be allowed to R.

EXAMPLE 3: Assume the same facts as in EXAMPLE 1, except that P purchased the mixing tanks under a contract that was treated as a binding contract under the rules in Regulation 17053.37-4. Assume further that 25 percent of P's total cost for the mixing tanks was actually paid prior to January 1, 2001, so that P's qualified cost for the mixing tanks was equal to 75 percent of the total cost of the tanks. Under these facts, since P's qualified cost under Regulation 17053.37-4 would be equal to 75 percent of P's total cost for the mixing tanks, R's qualified cost under this regulation could not exceed the amount of P's qualified cost, irrespective of the total amount paid by R to P to purchase the mixing tanks.

(6) *Lessor Reporting Requirement.* In the case of any lease treated as an operating lease under this regulation, the lessor shall provide the lessee with a statement within 45 days after the close of the lessee's taxable year for which the JSF Property Credit is allowable to the lessee. This statement shall contain the amount of the lessor's qualified cost (as calculated under this regulation) upon which the lessee is eligible to compute the JSF Property Credit and the amount of such qualified cost upon which the lessor has paid California sales or use tax. For purposes of providing this statement only, if a lessor is legally obligated to remit California sales or use tax with respect to its acquisition of qualified property, but has not yet remitted such amounts solely due to timing differences between the lessor's California sales and use tax return filing period and the lessee's taxable year, then the lessor may treat the amounts upon which the California sales or use tax liability arises as "qualified costs to the lessor." The statement required by this subsection of this regulation should not be filed with the lessee's tax return for the taxable year, but shall instead be made available to the Franchise Tax Board upon request.

(c) *Finance Leases.* In the case of any leasing transaction that is treated as a sale under Part 1 (commencing with Section 6001) of Division 2 of the Revenue and Taxation Code (relating to the payment and collection of California sales and use tax), the rules set forth in this subsection of this regulation shall apply. Any lease subject to the rules of this subsection of this regulation shall be referred to in this regulation as a "finance lease."

(1) *In General.* Under Revenue and Taxation Code Section 6006(g)(5), a lease of tangible personal property is generally treated as a sale for California sales and use tax purposes, unless the tangible personal property is leased in substantially the same form as acquired by the lessor or leased in substantially the same form as acquired by the transferor and the lessor or transferor has paid sales tax reimbursement or has paid use tax measured by the purchase price of the property. If the lease is not treated as a sale under Revenue and Taxation Code Section 6006(g)(5), then the rules of subsection (b) of this regulation apply.

(2) *Applicable Requirements.* In the case of a finance lease, the following requirements must be satisfied in order for the lessee to claim the JSF Property Credit.

A. *Lessee Must Be a Qualified Taxpayer.* The requirement under Regulation 17053.37-3 that the user of the qualified property must be a qualified taxpayer shall be applied to the lessee and not to the lessor.

B. *Use of Property in Qualified Activities.* The requirement under subsection (b)(4) of Regulation 17053.37-5 that property be used in qualified activities in order to be treated as qualified property shall be applied to the lessee and not the lessor with respect to the property that is the subject of a finance lease.

C. *Sales or Use Tax Payment Requirement.* Except as provided in subsection (d) of Regulation 17053.37-4 (relating to capitalized labor), either the lessor or the qualified taxpayer must pay California sales tax reimbursement or California use tax on the lessee's purchase of the qualified property in order for the JSF Property Credit to be allowed to the lessee. In the case of an "occasional sale" under Revenue and Taxation Code Section 6006.5, the lessee may satisfy the requirement of this subsection of this regulation by remitting the California sales or use tax on the lessee's purchase of the qualified property (assuming that under California sales and use tax law the lessor does not have a legal obligation to remit such amounts).

D. *Qualified Costs.* The requirement that costs, in order to be treated as qualified costs, must be paid or incurred for the "construction, reconstruction, or acquisition" of qualified property shall be applied by substituting the term "purchase" for the term "construction, reconstruction, or acquisition." Since under general income tax principles a finance lease is treated as a purchase, the lessee's "lease rental payments" are treated as payments of the purchase price of the qualified property and would thus satisfy the "purchase" requirement. However, the lessee under such a lease would be obligated to pay California sales or use tax at the time the lease became effective, so that the lessee would be allowed the entire JSF Property Credit on such lease in the year the lease became effective. On the other hand, if a lease is not properly treated as a finance lease under general income tax principles, then the "purchase" requirement would not be satisfied.

E. *Chargeable to Capital Account.* The requirement that costs, in order to be treated as qualified costs, must be properly chargeable to the capital account of the qualified taxpayer shall apply to the lessee's lease rental payments.

(3) *Amount of JSF Property Credit Lessee May Claim.* In general, a lessee under a finance lease is entitled to claim the JSF Property Credit at the same time and in the same amount as if such lessee had instead constructed, reconstructed, or acquired the qualified property other than by lease.

Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.

Regulation 17053.37-7

JSF Contract Bidding --(See Regulation 17053.37-0 for Table of Contents.)

(a) *In General.* The JSF Property Credit shall not be allowed unless the credit is reflected within the bid that forms the basis for the qualified taxpayer's contract or subcontract to manufacture property for ultimate use in a Joint Strike Fighter.

(b) *Bid.* For purposes of this regulation, the term "bid" shall mean a written bid or offer to perform a contract to produce a product that is physically attached to or installed in a Joint Strike Fighter, submitted to the United States government or the prime contractor, in response to a request for bids to construct all or a portion of the Joint Strike Fighter Aircraft. The bid shall be submitted in a competitive process where the contract will be awarded to the lowest possible bidder or as otherwise indicated in the conditions under which the bids will be received and the contract awarded.

(c) *JSF Property Credit Reflected Within the Bid.* For purposes of this regulation, the term "reflected within the bid" shall mean:

(1) the bid that forms the basis of the contract or subcontract is reduced by the amount of the JSF Property Credit allowable, and

(2) the amount of the JSF Property Credit allowable is included on the face of the bid or an attachment to the bid that forms the basis of the contract or subcontract.

The JSF Property Credit allowable shall be a lump sum number reflected on the contract or subcontract and the aggregate credit allowable over the term of the contract or subcontract is not required to be calculated on the basis of the year in which the credit amount is expected to be claimed.

EXAMPLE 1: X, a qualified taxpayer, submits a bid to the prime contractor in the amount of \$90 to manufacture retractable landing gear for the Joint Strike Fighter. The bid price without the JSF Property Credit would have been \$100. The bid form includes an attachment that states the JSF Property Credit allowable for the subcontract is \$10 (\$100 contract price less JSF Property Credit in the amount of \$10, for a reduced contract price of \$90). X is the successful bidder on the retractable landing gear and thereafter is awarded the contract to produce the part for the Joint Strike Fighter. X and the prime contractor execute a contract in the amount of \$90. Under these facts, the \$10 JSF Property Credit amount is reflected within the bid that forms the basis for X's subcontract to manufacture property for ultimate use in a Joint Strike Fighter and X may claim the \$10 JSF Property Credit if all of the other requirements of Section 17053.37 of the Revenue and Taxation Code and this regulation are met.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that the bid form reflects a price of \$100. In this circumstance, X is not eligible to claim the credit because X has not reduced the amount of the bid by the amount of the JSF Property Credit allowable.

EXAMPLE 3: Assume the same facts as in Example 1, except that the bid form reflects a price of \$90, but the bid form does not contain an attachment showing the amount of the JSF Property Credit allowable. In this circumstance, X is not eligible to claim the credit because

even though the bid amount has been reduced by the amount of the credit allowable, the amount of the credit allowable is not included on the face of the bid or in an attachment to the bid.

EXAMPLE 4: Assume the same facts as in EXAMPLE 1, except that the scope of the project changes after the bid is submitted and X and the prime contractor execute a contract in the amount of \$120, reflecting an increase of \$30 dollars in the original bid amount. In this circumstance, the cost for the expanded scope of the contract was added to the original bid amount. As a result, X would only be allowed to claim a \$10 JSF Property Credit since that amount was reflected within the original bid.

EXAMPLE 5: X, a qualified taxpayer, is the prime contractor awarded the initial contract from the United States government for the Engineering and Manufacturing Development Phase of the Joint Strike Fighter Program. X does not include any amount for the Joint Strike Fighter credit in its bid for the Engineering and Manufacturing Development Phase accepted by the United States government. Under these facts, X is not able to claim the JSF Property Credit since the credit amount was not reflected within the bid that formed the basis for the initial contract for the Engineering and Manufacturing Development Phase.

EXAMPLE 6: Assume the same facts as in Example 5, and Y responds to a request from X and submits a bid to subcontract a portion of the scope of the work covered in the Engineering and Manufacturing Development Phase of the Joint Strike Fighter Program. The bid form includes an attachment that shows the JSF Property Credit allowable for the subcontract is \$10 (\$100 contract price less JSF Property Credit in the amount of \$10 for a reduced contract price of \$90). Y is the successful bidder on that portion of the scope of the work and thereafter is awarded the contract to produce the part for the Joint Strike Fighter. X and Y execute a contract in the amount of \$90. Under these facts, the \$10 JSF Property Credit amount is reflected within the bid that forms the basis for Y's subcontract to manufacture property for ultimate use in a Joint Strike Fighter. Even though X, the prime contractor, did not reduce its bid for the prime contract and is not eligible to claim the JSF Property Credit, Y's bid met the bidding requirements for claiming the credit and Y may claim the \$10 JSF Property Credit if all of the other requirements of Section 17053.37 of the Revenue and Taxation code and this regulation are met.

(d) *JSF Property Credit Allowable.* For purposes of this regulation, the term "credit allowable" shall mean at the time the bid for the initial contract or subcontract is submitted, the amount of the credit the qualified taxpayer expects to claim as a result of qualified activities in connection with the contract or subcontract. The amount of the JSF Property Credit allowed to any qualified taxpayer under Section 17053.37 and these regulations shall not exceed the lesser of the credit amount reflected within the bid of the qualified taxpayer or the credit allowed for actual amounts paid or incurred by the qualified taxpayer.

EXAMPLE: Y, a qualified taxpayer, submits a bid to the prime contractor to manufacture the cockpit canopy for the Joint Strike Fighter. The bid form includes an attachment that shows the JSF Property Credit allowable for the subcontract is \$10 (\$100 contract price less JSF Property Credit in the amount of \$10 for a reduced contract price of \$90). X is the successful bidder on the cockpit canopy and thereafter is awarded the contract to produce this part for the Joint Strike Fighter. X and the prime contractor execute a contract in the amount of \$90.

Thereafter, Y's costs to produce the cockpit canopy increase by 10% and Y determines that its actual qualified costs would result in a JSF Property Credit in the amount of \$11. In this circumstance, even though Y's qualified costs have increased, Y is only able to claim a JSF Property Credit in the amount of \$10 since that is the amount of the credit allowable that was reflected within Y's bid.

(e) *Pass-Through Entities.* For purposes of this regulation:

(1) The amount of the JSF Property Credit allowable reflected on a bid submitted by a partnership or an S corporation shall be the amount of the JSF Property Credit expected to be passed through the partnership to the partners or through the S corporation to the shareholders in accordance with the applicable provisions of Part 10 (commencing with Section 17001) of the Revenue and Taxation Code.

EXAMPLE: Z, a qualified taxpayer, submits a bid to the prime contractor to manufacture a portion of the hydraulic system for the Joint Strike Fighter. Z calculates the total allowable JSF Property Credit to be \$75. Z has a valid S corporation election in effect for California tax purposes. Under Revenue and Taxation Code Section 23803(a)(1)(A), Z's JSF Property Credit is limited to one-third of the amount of the credit otherwise allowable (\$25). However, the amount of the JSF Property Credit that is expected to be passed through to Z's shareholders is \$75 and Z must reflect the \$75 reduced credit amount on the bid submitted to the prime contractor as provided in this regulation.

(f) *Copies Provided to Franchise Tax Board.* The qualified taxpayer shall provide, upon request of the Franchise Tax Board, a copy of any bid that forms the basis for a contract or subcontract to manufacture property for ultimate use in a Joint Strike Fighter.

Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.

Regulation 17053.37-8

Recapture Rules --(See Regulation 17053.37-0 for Table of Contents.)

(a) *In General.* The JSF Property Credit shall not be allowed or shall be recaptured under the rules of this regulation in any case where a disposition occurs within one year or less of the date the qualified property is first placed in service in this state.

(b) *Disposition.* For purposes of this regulation, the term "disposition" shall include any of the following events:

(1) Removal of the qualified property from this state;

(2) Disposition of the qualified property to any party that is not a related party (as defined in

Internal Revenue Code Sections 267, 318 or 707), whether by sale, gift, a transfer upon the foreclosure of a security interest, or otherwise;

(3) Use of the qualified property by the qualified taxpayer primarily in any non-qualified activity; or

(4) Acquisition by a lessee (or any party related to the lessee under Internal Revenue Code Sections 267 or 318) of qualified property that is being leased by such lessee.

However, the term "disposition" shall not include any of the following events:

A. a mere transfer of legal title to a creditor upon creation of a security interest;

B. a transfer by a qualified taxpayer of legal title to qualified property to a lessor where the lessor is not treated as the tax owner of such property and the lease is properly characterized as a financing transaction under California income tax principles;

C. any election by a C corporation to become an S corporation; or

D. any destruction of qualified property which qualifies as an involuntary conversion under Section 1033 of the Internal Revenue Code.

(c) *Disposition of Qualified Property During the Taxable Year Placed in Service.* In any case where there is a disposition of qualified property during the same taxable year in which such qualified property is first placed in service in this state, no JSF Property Credit shall be allowed to the qualified taxpayer for that property for the taxable year in which the qualified property is placed in service.

EXAMPLE: H, a qualified taxpayer, files its California tax returns using a fiscal year ending on September 30th. On March 1, 2001, H pays \$700 (plus California sales tax) for 10 personal computers and immediately places the computers in service in H's manufacturing facility in Burbank. On September 1, 2001, H acquires 10 new computers (which are immediately placed in service in H's manufacturing facility) for \$800 (plus California sales tax) to replace the 10 computers already in service, and H instead uses the old computers to perform general administrative functions such as payroll and marketing. Under these facts, when H files its California tax return for its taxable year ending September 30, 2001, H is not entitled to claim the JSF Property Credit for the 10 personal computers acquired on March 1, 2001, because the computers are treated as having been disposed of during the same taxable year as they were placed in service as a result of H's use of these computers in an activity that is not a qualified activity. However, the 10 new computers acquired on September 1, 2001, may qualify for the JSF Property Credit for H's taxable year ending September 30, 2001.

(d) *Disposition of Qualified Property During a Taxable Year Subsequent to the Taxable Year Placed in Service.* In any case where there is a disposition of qualified property within one year of the date that such qualified property is first placed in service in this state, but such disposition occurs in a different taxable year than the year in which the qualified property is

placed in service in this state, then any JSF Property Credit that was allowed with respect to the qualified property shall be recaptured by adding the recaptured JSF Property Credit to the tax of the qualified taxpayer for the taxable year during which the disposition occurs (except as provided in subsection (e) of this regulation).

EXAMPLE: F, a qualified taxpayer, files its California tax returns using a fiscal year ending on September 30th. On August 15, 2001, F acquires 20 new computers for \$600 (plus California sales tax) and immediately places the computers in service in H's manufacturing facility in Glendora. On May 15, 2002, F removes the 20 computers from F's manufacturing facility in Glendora and transports them for use in F's New Mexico manufacturing facility. Assuming F had been allowed a JSF Property Credit on its taxable year ending September 30, 2001, California tax return for the computers acquired on August 15, 2001, F must recapture the entire JSF Property Credit allowed by adding such amount to F's tax for its taxable year ending September 30, 2002.

(e) *Adjustment of Carryforwards when Disposition Occurs.* In any case where a qualified taxpayer is required to recapture any previously allowed JSF Property Credit under the rules of this regulation, then, prior to the addition of any recaptured amounts to the tax under subsection (d) of this regulation, any outstanding JSF Property Credit carryforwards shall first be reduced to the extent necessary to fully absorb the recapture amount. Any recapture amount remaining after application of the preceding sentence shall be added to the tax under the rules of subsection (d) of this regulation.

EXAMPLE 1: On May 1, 2002, within one year of placing qualified property in service in this state, K disposes of qualified property for which a \$150 JSF Property Credit was previously allowed. Under the rules of this regulation, K is required to recapture the entire \$150 JSF Property Credit. Assume K had \$400 in JSF Property Credit carryforwards that were available for use in 2002. Under these facts, K would reduce its available JSF Property Credit carryforwards to \$250 (\$400 minus \$150). Since no additional recapture amount remains, K is not required to increase its tax for 2002 to reflect the \$150 recapture amount.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that instead of \$400 in available JSF Property Credit carryforwards, K had only \$100 in available JSF Property Credit carryforwards. Under these facts, K would first reduce its available JSF Property Credit carryforwards to zero, and would then increase its tax for 2002 by \$50 (\$150 recapture amount less \$100 used to reduce available JSF Property Credit carryforwards).

(f) *Recapture of JSF Property Credit Allowed to Pass-Through Entities.*

(1) *Partnerships and Partners.* If a partnership places qualified property in service in this state, claims the JSF Property Credit to the extent of the qualified costs paid or incurred, and thereafter removes the qualified property from this state, disposes of the qualified property to an unrelated party, or primarily uses the property for a purpose not qualifying for the JSF Property Credit, then the JSF Property Credit shall be recaptured under Revenue and Taxation Code Section 17053.37(g) and this regulation. The amount of JSF Property Credit subject to recapture shall be allocated among the partners in the same ratio that the JSF Property Credit was allocable

to each partner for the qualified property subject to the recapture, and shall be added to the "tax" of the partner for the taxable year in which the qualified property is disposed of, removed from this state, or put to a non-qualifying use.

EXAMPLE 1: Assume that C and D are equal partners of M, a partnership that is a qualified taxpayer. During M's taxable year beginning in 2001, M is allowed a total JSF Property Credit of \$100. C and D each are able to utilize their entire 50% share of the 2001 JSF Property Credit to offset their respective 2001 tax liabilities, so that there is no JSF Property Credit carryover amount for either C or D. Assume further that in 2002, within one year of the date the qualified property was placed in service, M moves the qualified property to another state, thereby triggering a recapture of the JSF Property Credit. C and D are required to recapture their distributive share of the JSF Property Credit already applied to their respective 2001 tax liabilities on their respective 2002 California tax returns by adding the recaptured JSF Property Credit amounts to their respective "tax" for 2002.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that C uses all of C's share of the JSF Property Credit to reduce C's 2001 tax liability, but D carries over all of D's JSF Property Credit to 2002. On C's 2002 California tax return, C will be required to recapture C's share of the JSF Property Credit that was used to reduce C's "tax" for 2001 and D will be required to reduce its JSF Property Credit carryover to zero. D will not be required to increase D's "tax" for 2002 by the amount of D's share of the JSF Property Credit because D was unable to apply the amount to reduce D's tax liability for 2001.

(2) S Corporations and Shareholders.

A. Corporate Level Recapture. If an S corporation places qualified property in service in this state, claims the JSF Property Credit to the extent of the qualified costs paid or incurred, and thereafter removes the qualified property from this state, disposes of the qualified property to an unrelated party, or primarily uses the qualified property for a purpose not qualifying for the JSF, then the JSF Property Credit shall be recaptured under Revenue and Taxation Code Section 17053.37(g) and this regulation. The amount of any JSF Property Credit recaptured by the S corporation shall be added to the "tax" of the S corporation imposed under Chapter 4.5 of Part 11 of the Revenue and Taxation Code, except that the JSF Property Credit recapture amount added to the "tax" of the S corporation shall be appropriately reduced by the amount by which the S corporation was required to reduce such JSF Property Credit under Part 11 of the Revenue and Taxation Code.

B. Pass-through of JSF Property Credit Recapture Amount to Shareholders. In any case where a "disposition" of qualified property by an S corporation occurs, the amount of JSF Property Credit subject to recapture shall be allocated among the shareholders of the S corporation in the same ratio that the JSF Property Credit was allocable to each shareholder for the qualified property subject to the recapture, and shall be added to the "tax" of the shareholder for the taxable year in which the qualified property is disposed of, removed from this state, or put to a non-qualifying use.

EXAMPLE: Assume that Q, an S corporation with three equal shareholders (E, F, and G), is

allowed a JSF Property Credit in 2001 that Q is fully able to utilize to reduce Q's 1.5% S corporation tax liability. Assume further that E, F, and G each claims a one-third (1/3) share of the JSF Property Credit allowed to Q, and that each shareholder is able to utilize their entire distributive share of this JSF Property Credit on their respective 2001 California tax returns. In 2002, within one year of the date the qualified property was placed in service in California, Q sells the property to an unrelated party. Under these facts, Q, E, F, and G must each recapture the JSF Property Credit allowed and claimed by each on their respective 2001 California tax returns by adding such recapture amount to their 2002 respective California "tax" or "net tax," as the case may be.

Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.

Regulation 17053.37-9

JSF Property Credit Carryforwards --(See Regulation 17053.37-0 for Table of Contents.)

(a) *In General.* In any case where the JSF Property Credit exceeds the "tax," the excess may be carried forward to reduce the "tax" for the eight taxable years succeeding the taxable year for which the JSF Property Credit is allowed, if necessary, until the credit is exhausted.

(b) *Carryforwards for Pass-Through Entities.* In the case of any JSF Property Credit allowed to a pass-through entity, the determination of the applicable carryover period for any JSF Property Credit required to be carried forward shall be made at the pass-through entity level.

(c) *Carryforwards Permitted After Sunset.* For taxable years commencing on or after January 1, 2006, any unused JSF Property Credit may be carried forward, as provided above, until the unused JSF Property Credit is exhausted.

Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.

Regulation 17053.37-10

Recordkeeping Requirements -- (See Regulation 17053.37-0 for Table of Contents.)

(a) *In General.* For purposes of Regulations 17053.37-1 through 17053.37-11, inclusive, a qualified taxpayer shall be required to maintain books and records that are adequate to substantiate its entitlement to any claimed JSF Property Credit. These books and records should be retained for as long as the statute of limitations on assessment for the taxable year for which the JSF Property Credit was allowed remains open, and, in the case of any JSF Property Credit that is being carried forward, for the additional number of years that the actual carryforward of such JSF Property Credit occurs.

(b) *Books and Records.* The books and records maintained by the qualified taxpayer should be sufficient to clearly establish all necessary facts which affect the allowance and amount of the JSF Property Credit. For this purpose, "adequate" recordkeeping depends upon the sufficiency of the information contained in the documentation. In many cases, the books and records normally maintained for California income or franchise tax purposes will be adequate substantiation for the JSF Property Credit.

EXAMPLE 1: X, a qualified taxpayer, claims a JSF Property Credit for the purchase of 100 computers to be used in X's manufacturing facility in West Los Angeles. Assume the computers were purchased from a mail order retailer located in South Dakota. If X has only retained the original invoice and a cash disbursements journal, neither of which reflect that California sales or use tax was paid by X, then the invoice would not be sufficient to establish that California sales or use tax was paid on the computers. However, if X has retained a copy of a timely filed California use tax return that clearly demonstrates that California use tax was paid by X with respect to the computers, then X would be treated as having paid or incurred qualified costs.

EXAMPLE 2: Assume the same facts as in EXAMPLE 1, except that X intends to use 20 of the computers for general administrative functions such as payroll and marketing. In addition to the records necessary to establish that California sales or use tax was paid, X should also retain a copy of the purchase contract containing a detailed list of the computers by model number so that X can establish which of the computers are being used in qualified activities and which are not being used in qualified activities.

(c) *Affidavit Regarding Sales and Use Tax.* For purposes of this regulation only, in the case of any lump sum or turn key contract, the requirement that California sales or use tax be paid may be established by reference to bids, contracts or affidavits from the contractor. For purposes of determining whether California sales or use tax has been paid, directly or indirectly by the contractor, when it is not a separately stated contract amount, a qualified taxpayer shall be entitled to rely on a written representation to that effect from the contractor, and California sales or use tax shall be deemed to have been paid in the absence of affirmative knowledge on the part of the qualified taxpayer that California sales or use tax was not paid.

(d) *Written Statement by Lessor to Lessee.* In the case of any leasing transaction described in subsection (b) of Regulation 17053.37-6 (relating to operating leases), the lessor shall provide a statement to the lessee specifying the amount of the lessor's original cost of the qualified property upon which the lessee may claim the JSF Property Credit and the amount of that cost upon which California sales or use tax was paid. This statement must be provided to the lessee within 45 days after the close of the lessee's taxable year for which the JSF Property Credit is allowable to the lessee. For purposes of providing this statement only, if a lessor is legally obligated to remit California sales or use tax with respect to its acquisition of qualified property, but has not yet remitted such amounts solely due to timing differences between the lessor's California sales and use tax return filing period and the lessee's taxable year, then the lessor may treat the amounts upon which the California sales or use tax liability arises as "qualified costs to the lessor." This written statement should not be filed with any return of either the lessor or lessee, but shall instead be retained by the lessee and made available to the Franchise Tax Board

upon request.

Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.

Regulation 17053.37-11

Miscellaneous Provisions -- (See Regulation 17053.37-0 for Table of Contents.)

(a) *Effective Dates of the JSF.* The JSF Property Credit shall cease to be effective on December 1, 2006; however, any unused credit may be carried forward, as provided in Revenue and Taxation Code Section 17053.37(g) and Regulation 17053.37-9.

(b) *Manufacturers' Investment Credit (MIC).* Under Revenue and Taxation Code Section 17053.37, in any case where a credit would be allowed for qualified property under both that provision and the Manufacturers' Investment Credit (MIC) provided in Revenue and Taxation Code Section 17053.49, a qualified taxpayer may claim either the MIC credit or the JSF Property Credit. Thus, a qualified taxpayer may not claim both the JSF Property Credit and the MIC for the costs of the same qualified property.

(c) *Enterprise Zone Sales or Use Tax Credit.* Under Revenue and Taxation Code Sections 17053.37 and 17053.70, a qualified taxpayer that also operates in an Enterprise Zone may claim both the JSF Property Credit and the Enterprise Zone sales or use tax credit on the same item of qualified property to the extent that all of the requirements of each of those sections are satisfied.

Note: Authority cited: Section 17053.37(c)(3), Revenue and Taxation Code.

Reference: Section 17053.37, Revenue and Taxation Code.